No. 90-1029

In the
Supreme Court of the United States

OCTOBER TERM, 1991

EASTMAN KODAK COMPANY,
PETITIONER,
v.
IMAGE TECHNICAL SERVICES, INC., *et al.*,
RESPONDENTS.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

Brief Amicus Curiae of National Electrical Manufacturers Association in Support of the Petitioner

JAMES S. DITTMAR*
JAMES L. MESSENGER
WIDETT, SLATER & GOLDMAN, P.C.
Sixty State Street
Boston, Massachusetts 02109
(617) 227-7200

Counsel for Amicus Curiae National Electrical Manufacturers Association

**Counsel of Record*

Of Counsel:

DALE R. SCHMIDT
NATIONAL ELECTRICAL MANUFACTURERS ASSOCIATION
2101 L Street, N.W. Suite 300
Washington, D.C. 20037-1581
(202) 457-8400

BATEMAN & SLADE, INC. BOSTON, MASSACHUSETTS

Table of Contents

Table of Authorities Cited

CASES

Table of Authorities Cited
(Continued)

CASES

STATUTES

MISCELLANEOUS

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INTEREST OF AMICUS CURIAE

National Electrical Manufacturers Association ("NEMA") is this country's largest trade association for manufacturers of electrical equipment. NEMA's 630 member companies manufacture end-use equipment or components for the generation, transmission, control and use of electricity. NEMA's principal activities involve the development of domestic and interna-

tional standards, statistical and market programs, government relations and international trade.[1]

NEMA members are affiliated with one or more of the organization's divisions and sections. For example, NEMA members affiliated with its Diagnostic Imaging and Therapy Systems Division are engaged in the manufacture of complex, high-technology medical equipment such as computed tomography, magnetic resonance imaging, ultrasound, radiation therapy and nuclear medicine systems. NEMA members affiliated with its Industrial Control and Systems Section are engaged in the manufacture of electrical and electronic industrial control equipment such as industrial computers, programmable controllers and numerical control devices. NEMA members compete vigorously with respect to product quality and performance, and they spend substantial resources on research and development of systems and equipment, computer software, product upgrades and replacement parts. NEMA members compete in intense national and international interbrand markets for the manufacture, sale and service of their products.

NEMA is submitting this brief *amicus curiae* because the Court of Appeals erred in holding that Eastman Kodak Company ("Kodak") could have sufficient market power to support Sherman Act liability for tying under Section 1 or for monopolization or attempted monopolization under Section 2 when it is undisputed that Kodak lacks market power in the interbrand market for photocopier and micrographic equipment. The reasoning employed by the Court of Appeals implies that virtually every vertically integrated equipment manufacturer might be alleged to have market, or even monopoly, power in putative *single brand* after-markets of service or parts sales for its own equipment notwithstanding the absence of interbrand market power.

[1] This brief is filed pursuant to Rule 37 of the Rules of the Court, accompanied by the written consents of all parties.

NEMA believes that this case raises an important question of antitrust law and that the Court would benefit from the perspective of manufacturers that compete in national and international interbrand markets. A number of NEMA members either are at present, or have been in the past, involved in litigation raising the question which is dispositive of this case.

SUMMARY OF ARGUMENT

There are two critical, undisputed facts in this case, and these facts mandate a finding that Kodak could not possess market power in any putative after-market for parts or service. These facts are: (i) that Kodak does not have market power in the interbrand market for photocopier and micrographic equipment (Pet. App. 8A); and (ii) that customers consider the costs of subsequent service and parts[2] when making their initial decision to purchase such equipment (Pet. App. 8A, 20A). In light of these two undisputed facts, it follows inescapably that, if Kodak were to charge supercompetitive prices for parts or service, equipment purchasers would regard Kodak equipment as more expensive and would tend to buy the equipment offered by Kodak's interbrand rivals. If Kodak attempted to force an existing Kodak equipment owner to pay supercompetitive prices for parts or service, interbrand market forces (through the loss of market share which Kodak would suffer in the sale of new equipment) would force Kodak to reinstate

[2] Parts for products such as Kodak's copier and micrographic equipment and other complex, high-technology systems often include not only replacement parts identical to original components but also new features, software and even entire system upgrades (hardware and software) designed to provide an existing user with technology which is virtually identical to the product received by a current equipment purchaser.

competitive prices. Kodak simply cannot possess the market power necessary to support antitrust liability for its unilateral conduct in the putative after-markets, and the antitrust laws are not intended to proscribe unilateral conduct which is necessarily deterred and disciplined by market forces.[3]

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[3] NEMA is addressing at length only the question of whether the Court of Appeals erred in ruling that Kodak could possess market power in putative after-markets when it did not possess interbrand market power. This issue is sharply focused by the undisputed facts, highly important as a matter of antitrust law and dispositive of the case.

Nonetheless, the Court of Appeals seriously erred in a number of other respects as well. For example:

(i) The Court of Appeals ruled that "market imperfections" could contribute to market power in putative after-markets. (Pet. App. 10A.) The court erred because there was no record evidence, analysis or explanation of what these mysterious "market imperfections" were or of how they could have resulted in Kodak's having market power.

(ii) The Court of Appeals held that "[s]ome strength in the interbrand market, although short of actual market power, can combine with other factors to yield power in an after-market." (Pet. App. 12A.) The court erred because there is no legal significance to "strength" which falls short of "market power." The standard articulated by the court would leave a jury without principled guidelines and should therefore be rejected.

(iii) The Court of Appeals ruled that an integrated manufacturer may not package sales of equipment, parts or service because "it is a less restrictive alternative for Kodak to structure its prices for equipment, parts and service so that the price for which Kodak sells each of these reflects Kodak's investment costs in that area." (Pet. App. 14A.) The court erred because its ruling rests on a fallacious premise that an integrated manufacturer's "investment costs" in equipment, parts and service are distinct and separable.

(iv) The Court of Appeals ruled that *Aspen Skiing Co.* v. *Aspen Highland Skiing Corp.*, 472 U.S. 585, 605-08 (1985), requires a manufacturer to sell replacement parts to any purchaser if the manufacturer is without a "legitimate business justification" for refusal. (Pet. App. 16A.) The court erred because its application of *Aspen* improperly extends that precedent beyond the unusual circumstances of what was in economic substance a monopolist's termination of a joint venture with predatory intent. *Aspen* is only applicable if rivals are unable to duplicate the refused product. *See, e.g., Olympia Equipment Leasing Co.* v. *Western Union Telegraph Co.*, 802 F.2d 217, 219 (7th Cir. 1986). The Court of Appeals' improper reading of *Aspen* would eviscerate the longstanding principle that even a monopolist may unilaterally decline to deal with another party. *See, e.g., United States* v. *Colgate & Co.*, 250 U.S. 300, 307 (1919); Turner, *Anticipating Antitrust's Centennial: The Durability, Relevance, and Future of American Antitrust Policy*, 75 Calif. L. Rev. 797, 810 (1987).

ARGUMENT

I. The Court Of Appeals Erred In Holding That Kodak Could Have Sufficient Market Power To Support Liability In Putative Single Brand Parts Or Service After-Markets When Kodak Lacks Market Power In The Interbrand Market

— In order to prevail in a Section 1 tying case or a Section 2 case, plaintiff must establish that defendant possesses economic power. Market power requisite to Section 1 tying liability is the power to raise prices or to require purchasers to accept burdensome terms. *U.S. Steel Corp.* v. *Fortner Enterprises, Inc.*, 429 U.S. 610, 620 (1977); *see also Jefferson Parish Hospital Dist. No. 2* v. *Hyde*, 466 U.S. 2, 13-14 (1984). Monopoly power necessary to sustain a Section 2 claim is the power to control prices or exclude competition. *United States* v. *Grinnell Corp.*, 384 U.S. 563, 571 (1966). Monopoly power, of course, is something greater than market power. *Colorado Interstate Gas Co.* v. *Natural Gas Pipeline Co. of America*, 885 F.2d 683, 696 n.22 (10th Cir. 1989), *cert. denied*, 111 S. Ct. 441 (1990); *see generally* L. Sullivan, *Antitrust* § 22, at 75 (1977).

The Court of Appeals' holding that Kodak could possess market power in putative after-markets for parts or service should be reversed because the Court of Appeals' reasoning defies sound economic theory, is inconsistent with precedent and undercuts the antitrust laws' central objective of promoting interbrand competition. In his dissent (Pet. App. 19A-25A), Judge Wallace correctly observed that market forces necessarily prevent a manufacturer which lacks interbrand market power from possessing market power in putative single brand after-markets for service or parts. If Kodak attempted to raise its prices for service or parts to supercompetitive levels, or to

coerce customer action through tying service to parts, it would lose interbrand market share. Unless Kodak were to pursue a course of deliberate self-destruction, any truly anticompetitive conduct would be corrected by the market, and would in fact be deterred. The antitrust laws are not concerned with unilateral conduct which is necessarily checked by market discipline.[4]

Purchasers of complex, high-technology equipment such as Kodak office equipment seek out and consider, at the point of initial equipment purchase, information regarding quality and price of service and parts. These buyers make original equipment purchase decisions based on life cycle costs — that is, the costs of purchasing, maintaining and operating the equipment through its projected useful life. Consequently, vertically integrated manufacturers of such equipment compete fiercely with other manufacturers in the interbrand market with respect to the price and quality of service and parts as well as the price and quality of original equipment. Indeed, many manufacturers offer, and their customers often seek, extended parts and service warranties at the time of sale of the original equipment.

Due to competition in the interbrand market and the attentiveness of buyers to manufacturers' parts and service practices, purchasers of complex, high-technology equipment would respond to any manufacturer's anticompetitive parts or service practices. First, potential purchasers would alter their evaluation of the relative attractiveness of such a manufacturer's equipment. Second, present equipment owners adversely affected by a manufacturer's after-market conduct would alter their consideration of future equipment purchasing. Third, most manufacturers of complex, high-technology equipment offer more than one type of product to their customers. Consequently, a manufacturer's anticompetitive practice in one product market would also lead to loss of goodwill in other product markets.

[4]For example, market power sufficient to support antitrust liability is not established when low entry barriers and the presence of potential entrants would eventually discipline any present market participant that might attempt to charge supercompetitive prices. *See, e.g., United States* v. *Syufy Enterprises*, 903 F.2d 659, 664 (9th Cir. 1990); *see also Parts & Electric Motors, Inc.* v. *Sterling Electric, Inc.*, 866 F.2d 228, 236 (7th Cir. 1988), *cert. denied*, 110 S.Ct. 141 (1989) (Posner, J., dissenting) ("Even if Sterling had played this game, the result would have been a brief perturbation in competitive conditions — not the sort of thing the antitrust laws do or should worry about.").

The Court of Appeals' holding is inconsistent with past reasoning of the Court. Although the Court has not had the occasion, until now, to hold that a manufacturer that lacks interbrand market power cannot possess market power in a putative after-market for its own parts or service, the Court has recognized the competitive discipline which the interbrand market imposes on the pricing and distribution of a manufacturer's service or replacement parts. For example, in other contexts the Court has recognized the close interplay between the sale and the servicing of equipment and also the impact that the availability and quality of service can have on the original sale of a manufacturer's product. *Continental T.V., Inc.* v. *GTE Sylvania, Inc.*, 433 U.S. 36, 55 (1977). Likewise, the Court has recognized that the existence of interbrand competition provides a significant check on any attempt to exploit intrabrand competition. *Business Electronics Corp.* v. *Sharp Electronics Corp.*, 485 U.S. 717, 725 (1988); *see also Continental T.V.*, 433 U.S. at 51 n.17.

Lower courts have, in a similar vein, concluded that a vertically integrated equipment manufacturer which charges supercompetitive prices for parts or service, and thereby increases the life cycle costs of its equipment to noncompetitive levels, will lose interbrand market share. *See, e.g., General Business Systems* v. *North American Philips Corp.*, 699 F.2d 965, 972 (9th Cir. 1983); *Nobel Scientific Industries, Inc.* v. *Beckman Instruments, Inc.*, 670 F. Supp. 1313, 1323 (D. Md. 1986), *aff'd*, 831 F.2d 537 (4th Cir. 1987), *cert. denied*, 487 U.S. 1226, *reh'g denied*, 487 U.S. 1263 (1988).

The Court of Appeals' holding is also at odds with the Court's past observation that the "power" which a manufacturer has over its own brand-name or trademarked product is not power which creates an illegal monopoly when there are substitutes available. *United States* v. *E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 393 (1956). The power held by the manufacturer of a trademarked product derives from the product's reputation for quality, reliability and the like. That power is the natural and procompetitive consequence of product differentiation due to excellence. Such product differentiation is, of course, a hallmark of interbrand competition. To turn product differentiation in the interbrand market into market power in a putative single brand after-market, as the Court of Appeals has done, simply perverts *du Pont*'s teaching.

Indeed, the Court of Appeals' decision is inconsistent with the principal purpose of the antitrust laws — to protect interbrand competition. *Business Electronics*, 485 U.S. at 726. The Court of Appeals' decision not only misapplies antitrust law to parts and service practices of a vertically integrated manufacturer competing in an interbrand market; it also impairs the ability of the manufacturer to compete effectively in that market. The result reached by the court below would place the protection of individual competitors in a putative single product, intrabrand after-market above the fostering of vigorous competition in the interbrand market. The decision thus conflicts not only with the antitrust laws' purpose to protect interbrand competition; it similarly conflicts with the objective of protecting competition rather than individual competitors. *See, e.g., Brunswick Corp.* v. *Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977).

The "lock-in" theory relied on by the Court of Appeals as a possible source of market power reflects a gross misapplication of economic theory and antitrust law. The lock-in theory improperly focuses inquiry on customer choices at a point after

the sale of equipment instead of at the point of sale. Purchasers of complex, high-technology equipment are knowledgeable. They are often repeat customers for the same or related products; they communicate among themselves; they frequently retain consultants and review professional literature; and they listen to the comparative advertising arguments of both interbrand rivals and limited purpose competitors such as independent service organizations. These purchasers take into account parts and service prices and practices before they buy equipment. The lock-in theory simply has no legitimate application to purchasers of Kodak equipment.

Similarly, the Court of Appeals' reliance on the claimed uniqueness of Kodak parts as a possible source of market power is misplaced. The only meaningful test to determine whether a manufacturer possesses market power is whether it can raise prices profitably, exclude competition or require purchasers to accept burdensome terms. *Fortner Enterprises*, 429 U.S. at 620 n.13. While product uniqueness may in certain circumstances contribute to a manufacturer's market power, it does not establish the market power requisite to antitrust liability. *Jefferson Parish*, 466 U.S. at 37 n.7 (O'Connor, J., concurring). Because interbrand competition prevents Kodak from charging supercompetitive prices or coercing customers' service decisions, it is irrelevant that Kodak parts may be unique. Leading commentators thus have criticized those few courts which have held that the uniqueness of brand name replacement parts can form the basis of market power. P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 525, at 529-30 (1990).

Finally, for the same reason that a manufacturer of complex, high-technology equipment lacking interbrand market power cannot possess market power in a putative after-market for service or parts, in reality there can be no separate market for service or parts of a *single brand* of equipment. The def-

inition of a market must take into account the market participants' ability to raise prices or limit output and the extent to which substitutes put constraints on such ability. *Du Pont*, 351 U.S. at 394-400. An integrated manufacturer which raises parts or service prices to supercompetitive levels or which coerces customers' service decisions will lose its interbrand market share. Because the availability of interbrand substitutes thus precludes a manufacturer's ability to act independently of constraining consequences in the interbrand market, there simply can be no separate parts or service market for its *single brand* of product.

Following this reasoning, many lower courts have dismissed Section 2 claims against vertically integrated equipment manufacturers on the ground that there can be no separate market for the service and repair solely of their own products. *See, e.g., Nobel Scientific Industries*, 670 F. Supp. at 1322-23; P. Areeda & H. Hovenkamp, *Antitrust Laws* ¶ 525, at 530 (citing cases).

The absence of a product market for Kodak parts or for service of Kodak equipment that is distinct from the interbrand equipment market also dooms the tying claim under Section 1. As the Court confirmed in *Jefferson Parish*, 466 U.S. at 21, "a tying arrangement cannot exist unless two separate product markets have been linked." As Justice O'Connor, writing for four Justices, also concluded:

> For products to be treated as distinct, the tied product must, at a minimum, be one that some consumers might wish to purchase separately *without also purchasing the tying product*. When the tied product has no use other than in conjunction with the tying product, a seller of the tying product can acquire no *additional* market power by selling the two products together.

Id. at 39 (emphasis in original) (citations omitted). Here, the threshold prerequisite for a tying claim — the existence of two separate product markets — is not satisfied. The provision of Kodak parts and service cannot be viewed in isolation from the sale of Kodak equipment. Interbrand competition reveals the artificiality of the effort to separate markets for original equipment, parts and service of a single brand. After considering the costs of equipment, parts and service together, customers purchase Kodak parts and service only because they elect to purchase Kodak equipment. Parts and service, thus, are inseparable from the original equipment purchase. There is no such thing as a single brand, or intrabrand, parts or service market.

II. The Court Of Appeals' Decision Will Impede Procompetitive Business Practices And Effective Interbrand Competition

The Court of Appeals' decision will compel equipment manufacturers either to sell parts to purchasers such as independent service organizations or to incur the costs and risks of treble-damage lawsuits. The decision will limit the flexibility of manufacturers to devise parts and services strategies to meet the demands of a competitive marketplace, and the impairment of that flexibility will undermine interbrand competition. The decision will also weaken interbrand competition by depriving manufacturers of the ability to control the quality of their own products.

Manufacturers of complex, high-technology equipment compete by virtue of quality as well as price. Quality is determined by the design and manufacture of the product, the design and installation of parts and the servicing of the equipment. Improper installation of parts or low quality servicing can

affect the performance of the entire integrated system. In order to ensure the quality of their products, accordingly, manufacturers may choose to control parts installation and service.[5]

An equipment manufacturer may also elect to restrict the sale of parts to third parties in order to preclude the "finger-pointing" which is likely to result when the manufacturer loses control over parts and service. Because the purchaser cannot independently distinguish poor service or improper parts installation from malfunctioning of the original equipment or its parts, the purchaser generally holds the manufacturer responsible for equipment or parts failures. Indeed, an independent service organization has a virtually irresistible temptation to blame the manufacturer for every product performance problem, including problems caused by the service organization's own improper installation of parts or its flawed servicing of the system. Finger-pointing thus detracts from the equipment manufacturer's ability to compete on the basis of quality, because it denies the manufacturer the certainty that its investment in the quality of its equipment and parts will be reflected in the performance of its product. Finger-pointing also inherently impairs the ability of the marketplace to properly reward, and also punish, manufacturers for what is done by them rather than for what is done by someone else.

Lost control over the distribution of parts and service can also discourage manufacturer offerings of warranties and of reduced prices for parts. Because improper installation and service of parts can affect performance, an equipment manufacturer may reasonably fear that exposure under parts warranties or through product liability claims will increase if it must sell

[5]Of course, a manufacturer may also wish to permit, or even encourage, customers' use of independent service organizations. The point is that the manufacturer should be afforded the flexibility to decide how best to respond to its customers' needs and the conditions prevailing in the interbrand market.

to independent service organizations that it does not control. The consequence is an undermining of the manufacturer's incentive to offer warranty protections.[6]

The purpose of the antitrust laws is to protect competition in order to promote product innovation, improvement in quality, increase in output and reduction in total costs. *See, e.g., National Society of Professional Engineers* v. *United States*, 435 U.S. 679, 695 (1978). The decision of the Court of Appeals improperly frustrates that purpose by restricting the flexibility of, and undermining the rewards available to, equipment manufacturers that compete in the interbrand market on the basis of the quality of their equipment or on the basis of the warranty protections offered to their customers.

[6]Even assuming that a manufacturer may have market power with respect to sale of its parts, the economic efficiencies and justifications which are often associated with refusals to sell parts demonstrate that the time is ripe for the Court to abandon the per se rule in tying cases. *See Jefferson Parish*, 466 U.S. at 40-41 (O'Connor, J., concurring).

CONCLUSION

The judgment of the Court of Appeals should be reversed and the summary judgment entered by the District Court should be reinstated.

Respectfully submitted,

JAMES S. DITTMAR*
JAMES L. MESSENGER
WIDETT, SLATER & GOLDMAN, P.C.
Sixty State Street
Boston, Massachusetts 02109
(617) 227-7200

Counsel for Amicus Curiae
National Electrical
Manufacturers Association

**Counsel of Record*

Of Counsel:

DALE R. SCHMIDT
NATIONAL ELECTRICAL
MANUFACTURERS ASSOCIATION
2101 L Street, N.W. Suite 300
Washington, D.C. 20037-1581
(202) 457-8400

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